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IN THE

SUPREME COURT OF THE UNITED STATES

No. 77. October Term, 1938.

GUY H. HELVERING, COMMISSIONER OF INTERNAL REVENUE,

vs.

FRANK PARDEE, ARIO PARDEE, and GIRARD TRUST COMPANY, TRUSTEES UNDER THE WILL OF CALVIN PARDEE,

Respondent.

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

Brief for the Respondent.

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BRIEF FOR THE RESPONDENT.

OPINIONS BELOW.

The opinion of the Board of Tax Appeals (R. 23) is reported in 23 B. T. A. 846. The opinion of the Circuit Court of Appeals (R. 34) is reported in 63 F. (2d) 948.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered March 4, 1933 (R. 36). The petition for a writ of certiorari was filed May 17, 1933, and was granted May 29, 1933 (R. 38). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

ARGUMENT

Calvin Pardee, a resident of Pennsylvania, by his will gave his residuary estate in trust to pay to his widow an annuity of $50,000, and to divide the remaining income among his children and issue of deceased children, with ultimate remainders not important here.

Under the law of Pennsylvania the annuity to the widow was payable primarily out of income, but in case of a deficiency in income, the deficit was payable out of principal. (*Johnston's Estate*, 264 Pa. 71.)

Under the decision of this Court in *Burnet v. Whitehouse*, 283 U. S. 148, payments received by the widow on account of her annuity, whether out of income or principal of the estate, were not taxable to her because exempt under Section 213 (b) (3) of the 1924 Revenue Act, which provides that the term "gross income" does not include the value of property acquired by gift, bequest, devise or descent.

For the taxable years in question, 1924 and 1925, payments to the widow were in fact made out of income of the estate, and in computing the taxable income of the estate the trustee deducted the amount so distributed to the widow under the authority of Section 219 (b) (2) of the 1924 Revenue Act, which provides:

> "There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not."

It will be seen, therefore, that the whole point of the case turns upon the question whether a widow who receives an annuity is a beneficiary within the meaning of the Act.

It must be assumed that when Congress used the word "beneficiary" it did so in the ordinary and commonly accepted meaning of the word. (*Old Colony R. Co. v. Commissioner of Internal Revenue*, 284 U. S. 552, at p. 560.)

In common parlance the word "beneficiary", as applied to a decedent's estate, means any one who receives a share of the estate, whether it be income or principal. It is defined by the Regulations promulgated by the Commissioner, under the 1924 Act, as follows:

> "The term 'beneficiary' as used in this article includes any person entitled to an interest in the income or the principal of a trust, but does not include one having merely a nominal interest in the income or principal. (Reg. 65, Art. 347)."

Manifestly the widow in this case is a beneficiary in the ordinary meaning of the word. The petitioner, however, contends that Congress intended the word "beneficiary" to include only those beneficiaries who are, under the Act, subject to tax upon the amounts of income so distributed. This contention is urged upon two grounds,

(1) That this Court has already so decided in *Burnet v. Whitehouse*, supra; and

(2) That under Section 219 (b) (2) the deduction allowed for amounts distributed to the beneficiaries is conditioned upon the inclusion of such amounts in computing the net income of the beneficiaries.

1. The question before this Court in *Burnet v. Whitehouse* was not whether in computing the taxable income of an estate the trustees were entitled to deduct payments of income made to an annuitant, but whether such payments were taxable to the annuitant simply because they happened to be made out of the income of the estate. This Court held that a fixed annuity was property acquired by gift, bequest, devise or descent, and therefore exempt from tax to the annuitant under provision of Section 213 (b) (3) of the Revenue Act of 1921, which is the same as the corresponding section of the 1924 Act.

Section 219 of the 1921 Act contained a provision similar to that in Section 219 of the 1924 Act, and the Commissioner in that case argued that under that section payments made on account of the annuity, insofar as they were made from the income of the estate, were taxable to the annuitant. This Court, however said, (p. 151):

> "But clearly enough, we think, this section applies only to income paid as such to a beneficiary. And, as above shown, the sums received by Mrs. Whitehouse were not gifts to be derived from and paid out of income, *nor were they received as such by her.*
>
> "The exemption in Section 213 is plain and should not be destroyed by any strained construction of general language found in Section 219."

It seems quite clear that all the Court intended to say in that case was that, regardless of the fact that payments were made out of income, they did not represent income to the annuitant.

Referring to Section 219 (b) (2) it will be observed that the deduction which is allowed to the estate is "the amount of the *income of the estate* * * * which is to be distributed currently by the fiduciary to the beneficiaries."

Clearly the right to deduct depends solely upon the fact that the payments are made out of the income of the estate, and it is immaterial that when they get into the hands of the beneficiary they may not represent income or taxable income to her.

2. This brings us to the second ground for petitioner's contention, namely, that the deduction is allowed to the trustees only on condition that the beneficiaries pay the tax.

This would be a strained construction of this section. Obviously the provision "but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries, whether distributed to them or not" is not a condition of the deduction allowed to the trustees. The sole purpose of this clause was to require the beneficiaries to include, in computing their individual net income, any income which they were entitled to receive for the taxable year, *whether in fact distributed or not.*

The petitioner says that Congress intended to tax all income accruing to property held in trust, and that if the income paid to the widow in this case is not taxable to the trustee, it will be exempt from tax altogether.

It is for Congress and not for the Courts to determine what income shall be taxed and what shall be exempt. While it is true that the exemption from tax in cases such as this may mean a substantial loss of revenue to the Government, that is a legislative, and not a judicial matter.

The intention of Congress must be derived from the language which it used. As Judge Woolley said in the opinion in the court below in No. 75, referring to this argument:

> "The infirmity in this argument is that taxation is not imposed by reasoning or by an exigency but by statute and only those named in the statute must

pay a tax. If in naming taxables it should, as here, later be found that the Congress, (for whatever reason) omitted a class available for taxation, that is a misfortune of the government which cannot be cured by a court reading into a statute something which is not there, or giving its words a meaning different from their known and ordinary signification."

The petitioner also argues that Congress did not intend to create an exemption in favor of income distributed to widows. However that may be as a general proposition, this Court has said in the *Whitehouse* case that where income is distributed to a widow on account of a fixed annuity, Congress plainly intended that such income should be exempt.

The fallacy of the petitioner's position is that it assumes that Congress intended to tax all income, whereas, obviously, such is not the case. For instance, income paid on account of charitable bequests is exempt from tax to the beneficiary, but is not on that account taxable to the trustee. (*Lederer v. Stockton*, 260 U. S. 3.) It is quite reasonable to suppose that when Congress made an exemption in favor of property acquired by gift, bequest, devise or descent it meant to grant an absolute exemption in favor of such property, regardless of the source from which payment happened to be made, and that this was the intention is confirmed by the fact that after the decision of this Court in the *Whitehouse* case, Congress, in Section 162 of the 1932 Revenue Act, re-enacted the provisions of Section 219 (b) (2) of the 1924 Act without change.

In the *Butterworth* case, (No. 75) the petitioner's principal argument is that under Section 219 (b) (2), the income is taxable to the widow. While this argument cannot prevail in this case, in view of this Court's decision in the *Whitehouse case*, it is a virtual admission that

the interpretation upon which petitioner relies in this case is untenable, since it would be absurd to say that a widow who receives an income for life is a beneficiary, but a widow who receives an annuity for life is not.

The fallacy of the petitioner's argument is further illustrated by carrying it to its logical conclusion. Assume that the net income of the Pardee estate in a given year was exactly $50,000., so that the entire income was paid to the widow. If the trustee is required to pay the tax, it has no source of payment but principal, in which case the tax would be a tax on principal, which, as petitioner points out, would be unconstitutional. Moreover, it is not by any means fanciful to imagine that such a tax, through a period of years, might so reduce the principal that the estate would be insufficient to pay the widow's annuity, so that the tax would finally fall upon her. Certainly such an iniquitous result is not to be ascribed to Congress unless the language of the taxing act admits of no possible alternative.

Respectfully submitted,

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